

**Letter of Findings: 07-0147
Indiana Individual Income Tax
For 2003 and 2004**

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ISSUE

I. Rent Expense – Adjusted Gross Income Tax.

Authority: IC § 6-8.1-5-1(b); I.R.C. § 280A(a); I.R.C. § 280A(c)(1).

Taxpayer challenges the Department of Revenue's decision disallowing a rental deduction.

STATEMENT OF FACTS

Taxpayer is sole owner of an automobile dealership. The dealership is incorporated in Indiana and elected to be treated as an S corporation for federal and state income tax purposes.

The Department of Revenue (Department) conducted an investigation of taxpayer's individual income tax returns for 2003 and 2004. Because the dealership was an S corporation, the investigator noted that all income and expenses flowed through to taxpayer as the sole shareholder.

The investigation report made a number of adjustments, one of which the taxpayer protested. An administrative hearing was conducted, and this Letter of Findings results.

I. Rent Expense – Adjusted Gross Income Tax.

DISCUSSION

Taxpayer purchased a condominium in Chicago. The dealership made monthly mortgage payments on the condominium and claimed the mortgage payments as a rental expense on the dealership's return. The investigation report disallowed the claimed expenses. Taxpayer explained that he made weekly trips to Chicago and vicinity in order to purchase vehicles for his business. Which in Chicago, taxpayer stayed in the condominium. In lieu of paying for a hotel room, taxpayer claims that the mortgage payments represent an ordinary and necessary business expense which should not have been disallowed on the S corporation's returns.

Pursuant to IC § 6-8.1-5-1(b), the taxpayer has the burden of demonstrating that the proposed assessment is incorrect. "The notice of proposed assessment is prima facie evidence that the department's claim for the unpaid tax is valid. The burden of proving that the proposed assessment is wrong rests with the person against whom the proposed assessment is wrong." *Id.*

It is not disputed that the Indiana tax returns for the tax years 2003 and 2004 employ federal adjusted gross income as the starting point for determining a taxpayer's state individual income tax liability.

I.R.C. § 280A(a) provides that, "Except as otherwise provided in this section, in the case of a taxpayer who is an individual or an S corporation, no deduction otherwise allowable under this chapter [IRC Sections 1 et seq.] shall be allowed with respect to the use of a dwelling unit which is used by the taxpayer during the taxable year as a residence."

I.R.C. § 280A(c)(1) provides an exception to the limitation as follows:

Subsection (a) shall not apply to any item to the extent such item is allocable to a portion of the dwelling unit which is exclusively used on a regular basis (A) as *the principal place of business for any trade or business of the taxpayer*, (B) as a place of business which is used by patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of his trade or business.... (*Emphasis added*).

Taxpayer contends that the condominium is used for a business purpose because taxpayer stays in the condominium at the time that he is purchasing automobiles for his dealership. In addition, taxpayer states that during the time that he stays at the condominium, taxpayer is reviewing his dealership's paperwork and records.

The Department has no reason to doubt taxpayer's contention that his use of the Chicago condominium is tangentially related to his business trips. However, taxpayer has not met his burden of demonstrating that the condominium functions as the taxpayer's "principal place of business."

Taxpayer also contends that the mortgage payments are simply the equivalent economic substitute for the hotel expenses he would otherwise incur if he did not own the condominium and that – presumably – taxpayer would be entitled to claim the hotel charges as a legitimate business expense. The Department finds no statutory authority for such an argument. Business hotel expenses are fundamentally different from mortgage payments on a condominium because the payments made for a hotel stay do not represent an investment in the equity of the property. The Department cannot agree that an investment in real property constitutes an ordinary and necessary business expense.

FINDING

Taxpayer's protest is respectfully denied.

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